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CENTRAL ILLINOIS PUBLIC SERVICE :  
COMPANY :  
d/b/a AmerenCIPS and :  
UNION ELECTRIC COMPANY :  
d/b/a Ameren UE :

Docket No. 02-0656

Petition for approval of tariff sheets :  
implementing revised Market Value Index :  
methodology :

Commonwealth Edison Company :

Proposed revision of Rider PPO (Power :  
Purchase Option - Market Index), Rate :  
CTC (Customer Transition Charge) and :  
Rider ISS (Interim Supply Service), and to :  
Establish Rider CTC - MY (Customer :  
Transition Charge - Multi-Year :  
Experimental) :

Docket No. 02-0671

ILLINOIS POWER COMPANY :

Proposed establishment of Rider MVI II, :  
(Market Value Index II) :

Docket No. 02-0672

INITIAL BRIEF OF THE  
NATIONAL ENERGY MARKETERS ASSOCIATION

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<b>(Market Value Index II)</b>	:	

**INITIAL BRIEF OF THE  
NATIONAL ENERGY MARKETERS ASSOCIATION**

**I. Introduction**

This Initial Brief is submitted by The National Energy Marketers Association ("NEM") in the above-referenced proceeding. NEM is a national, non-profit trade association representing wholesale and retail marketers of energy, telecom and financial-related products, services, information and related technologies throughout the United States,

Canada and the U.K. NEM's Membership includes wholesale and retail suppliers of electricity and natural gas, independent power producers, suppliers of distributed generation, energy brokers, power traders, and electronic trading exchanges, advanced metering and load management firms, billing and information technology providers, credit, risk management and financial services firms, software developers, clean coal technology firms as well as energy-related telecom, broadband and internet companies.

This regionally diverse, broad-based coalition of energy, financial services and technology firms has come together under NEM's auspices to forge consensus and to help resolve as many issues as possible that would delay competition. NEM members urge lawmakers and regulators to implement:

- Laws and regulations that open markets for natural gas, electricity and related products, services, information and technology in a competitively neutral fashion;
- Rates, tariffs, taxes and operating procedures that unbundle competitive services from monopoly services and encourage true competition on the basis of price, quality of service and provision of value-added services;
- Competitively neutral standards of conduct that protect all market participants;
- Accounting and disclosure standards to promote the proper valuation of energy assets, equity securities and forward energy contracts, including derivatives; and
- Policies that encourage investments in new technologies, including the integration of energy, telecommunications and Internet services to lower the cost of energy and related services.

NEM submits this Brief to urge the Commission to adopt market value calculation methodologies that more fully reflect both the legislative intent and prior Commission rulings on the issue. NEM specifically urges the Commission, at a minimum, to adopt the modifications to the market value index calculation that would result in at least a 15 mill upward adjustment to the market value index.

## A. Statutory Provisions

The processes for the determination of market value are set forth in Section 16-112 of the Public Utilities Act. Section 16-112(a) provides that,

The market value to be used in the calculation of transition charges as defined in Section 16-102 shall be determined in accordance with either (i) a tariff that has been filed by the electric utility with the Commission pursuant to Article IX of this Act and that provides for **a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy**, or (ii) in the event no such tariff has been placed into effect for the electric utility, or in the event such tariff does not establish market values for each of the years specified in the neutral fact-finder process described in subsections (b) through (h) of this Section, a tariff incorporating the market values resulting from the neutral fact-finder process set forth in subsections (b) through (h) of this Section. (emphasis added).

Furthermore, Section 5/16-112(k) provides that,

In determining the market values to be used for the various customer classes in calculating transition charges as defined in Section 16-102 or for the power purchase options set forth in Section 16-110, **an electric utility shall apply the market values that are determined as set forth in subsection (a) to the electric power and energy that would have been used to serve the delivery services customers' electric power and energy requirements, based on the usage specified in Section 16-102 and taking in to account the daily, monthly, annual and other relevant characteristics of the customers' demands on the electric utility's system**. (emphasis added).

Accordingly, as more fully explained below, the statute contemplates that the market value calculation is to be reflective of the retail cost of serving customers, not merely the wholesale cost. The statute further contemplates that the utilities have an affirmative obligation to maximize the value of capacity remaining when customers migrate to competitive suppliers and also have a corresponding obligation to shed, or avoid, the costs of serving the customers that have migrated.

The Commission's authority with respect to the approval of market value index tariffs is set forth in Section 16-112(m) that provides that,

The Commission may approve or reject, or propose modifications to, any tariff providing for the determination of market value that been proposed by an electric utility pursuant to subsection (a) of this Section, but shall not have the power to otherwise order the electric utility to implement a modified tariff or to place into effect any tariff for the determination of market value other than one incorporating the neutral fact-finder procedure set forth in this Section. Provided, however, that if each electric utility serving at least 300,000 customers has placed into effect a tariff that provides for a determination of market value as a function of an exchange traded or other market traded index, options or futures contract or contracts, then the Commission can require any other electric utilities to file such a tariff, and can terminate the neutral fact-finder procedure for the periods covered by such tariffs.

Pursuant to the above-referenced Section, the Commission has the authority to review and propose modifications to the utilities proposed market value index tariffs. However, the Commission cannot compel the utilities to implement modified tariffs unless said tariffs utilize the neutral fact-finder procedure.

#### **B. History of the Market Value Process**

The Commission previously approved market value index tariffs for Commonwealth Edison, Illinois Power, and Ameren in Cases 00-0259, 00-0395 and 00-0461. However, the Commission's approval of these tariffs was conditional. In view of a number of concerns expressed by the parties to the proceeding, including the potential understatement of the market value, the Commission found it was, "not prepared at this time to authorize the utilities to permanently put their market value tariffs in place, even as modified by the Commission proposals contained in this order." (Cases 00-0259, 00-0395, 00-0461, Order on Reopening, issued April 11, 2001, page 157). Accordingly, the

approved tariffs were to, "cease to be effective no later than the conclusion of the customer's May, 2004 billing period," and the utilities were to file new proposed market value tariffs on or before October 1, 2002. (Cases 00-0259, 00-0395, 00-0461, Order on Reopening, issued April 11, 2001, page 157). Therefore, this proceeding should properly entail a full and thorough examination of the propriety of the utilities' proposed market value index tariffs.

### **C. Summary of Position and Recommendations**

NEM urges that the Commission should adopt, at a minimum, a 15 mill upward adjustment to market value calculation methodologies. In the absence of a fully allocated embedded cost study to determine the full energy supply and commercial costs of serving retail load, and given the accretive nature of these costs, NEM submits that it is entirely proper for the Commission to adopt a market value adjustment of at least 15 mills pursuant to the analysis of the RES Coalition. In fact, it is NEM's experience from other jurisdictions that a larger adder of 2.0 to 2.5 cents/kWh could be more appropriate and justifiable. NEM submits that if the Commission wishes to foster a robust, competitive market, it must at a minimum, adopt the 15 mill upward adjustment. Anything less than the magnitude of 15 mills will ensure either stagnance or a possible reversal of a competitive market in Illinois.

NEM submits that market values must be priced at retail rates. If the market value is subsidized or set artificially low, i.e., if it does not reflect the true costs of providing retail generation and related services, true competition on the basis of price and quality of service will not be possible. If the market value is set artificially low the transition

charge will be artificially high. Conversely, if the market value is set artificially low the purchase power option price will also be set artificially low. Competitive suppliers will be challenged to cover their costs and offer products that provide value to customers. If the incumbent utility is permitted to subsidize retail energy services by passing through wholesale price signals and embedding the retail costs of energy-related products, services, information and related technologies in its distribution rate, a competitive marketplace cannot occur. Establishing a market value index in such a fashion not only distorts energy price signals but establishes a significant barrier to effective price competition by forcing customers who switch to competitive suppliers to pay twice for retail energy services. Under these circumstances fewer customers will choose competitive energy service providers, the utility's market share will be maintained, consumers will not benefit to the degree they should, and competitive markets simply won't develop.

The RES Coalition has offered a number of recommended modifications to the market value index calculation with a resultant upward increase in the market value calculation of 15 mills which more fully reflects the commercial costs and energy-related costs of serving retail load. As explained by RES Coalition Witnesses Gale and O'Connor,

(t)he RES Coalition, through a multi-method approach, has identified a residual relative to the MVI currently in place of over two-fifths or approximately 15 mills or 1.5¢/kWh relative to the actual value of power and energy for retail service. This is the extent to which the current MVI under-prices the Market Value of Energy Charge ("MVEC") in relation to the observed market value of energy in ComEd's retail service market. (Direct Testimony of Brent Gale and Philip O'Connor, page 6, lines 122-130).

The total 15 mill adjustment results from a number of proposed structural changes to the market value calculations, resulting in a 7 mill increase, as well as the following utility-specific recommendations,

For the Illinois Power service territory, the RES Coalition recommends that the Commission direct IP to adopt a "floating adder" approach, that appropriately addresses the operations barriers that continue to frustrate competitive development.

...

the ComEd and Ameren calculations [should] include an upward adjustment of approximately 8 mills per kilowatt hour (\$0.008/kWh) or about one-third of current MVI value. (Direct Testimony of Brent Gale and Philip O'Connor, pages 32-33, lines 710-723, 729-733).

NEM urges the Commission, at a minimum, to adopt the 15 mill upward adjustment in order to effectuate the legislative intent of the market value calculation provisions of the electric choice law as well as previous Commission Orders deciding that market value calculations should be reflective of the costs of serving retail customers.

NEM also urges that customer eligibility for ComEd's Rider CTC-MY should be expanded as suggested by the RES Coalition.

## **II. Proposed Adjustments or Revisions to Utilities Proposals**

### **D. Other**

The importance of properly determining market value is critical to the development of the competitive market in Illinois. As explained by RES Coalition Witnesses Gale and O'Connor,

If the market value is set too high, transition charges will be set too low. All things being equal, this would likely result in a large number of retail customers choosing alternative suppliers and, consequently, the utility would be unable to sell electricity at volumes and prices reflected in



designing its transition charges. In short, the utility would likely experience an undue revenue shortfall.

Conversely, if market value is set too low, transition charges will be set too high. All things being equal, this would likely result in virtually all retail customers being served by the utility under historical bundled service or under the Power Purchase Option ("PPO"). In short, competition would flounder and, in fact, could cease to exist because alternative suppliers would be unable to compete against the incumbent utility's price for electric power and energy.

Given this delicate balance, it is critical that the market value reflects the true cost of serving retail customers. (Direct Testimony of Brent Gale and Philip O'Connor, page 13, lines 291-305).

In the previous market value index cases, the Commission reaffirmed that market value is to be expressed in terms of the retail, not wholesale, market. The Commission found that,

On the issue of the appropriate market, the Commission believes that the General Assembly intended for the market value, which is determined pursuant to Section 16-112 of the Act, to represent the value of power and energy at the retail level. This is consistent with the Commission's interpretation of the statute as a whole and with the Commission's previous findings related to market value. The Commission's view is that when the definition of transition charges in Section 16-102 of the Act is read along with Section 16-110, which relates to the PPO, and Section 16-112 of the Act which explains how market value is to be determined, **it is clear that market value is not intended to reflect the wholesale market value.** The Commission notes that the same issue arose previously in the utilities' delivery services proceedings. On this point, the Commission previously found, "**It is clear to the Commission that the General Assembly contemplates that the market value may include costs associated with retail marketing costs.**" (emphasis added). (Docket Nos. 99-0120/99-0134, Order at 109-110). Cases 00-0259, 00-0395, 00-0461, Order on Reopening, issued April 11, 2001, page 164.

NEM submits that the market value for electricity should include the full energy supply and commercial costs of serving retail load including transmission charges, scheduling and control area services, and distribution system line losses, a share of pool operating

expenses, risk management premiums, load shape costs, commodity acquisition and portfolio management, working capital, taxes, administrative and general expenses, the costs of metering, billing, collections, bad debt, information exchange, compliance with consumer protection regulations, and customer care. NEM urges the Commission to again reject the utilities' arguments that would improperly account only for wholesale energy market values in the market value calculation. Furthermore, inherent in the statutory concept of "market value" is the requirement that the utilities maximize the value of capacity that is not utilized when customers migrate to competitive suppliers and that utilities must productively manage and mitigate costs that can and should be avoided when customers migrate. An adder of at least 15 mills would minimally approximate the values that should be included in a market value index calculation according to the intent of the Illinois legislation and prior Commission Orders on this issue.

The RES Coalition advocates a 15 mill adjustment to the market value calculation that is intended to address (and NEM maintains only partially) the undervaluation of the current market value index. (Direct Testimony of Brent Gale and Philip O'Connor, page 6, lines 122-130).

The 15 mill adjustment is comprised of an 8 mill adder and technical and structural modifications to the MVI that yield a 7 mill increase. RES Coalition Witnesses Bollinger, Goerss and Spilky explain that the modifications are justified because, "the MVI methodologies do not capture costs associated with imbalance risk management, 'odd lots,' peak demand coinciding with peak prices, sales and marketing expenses, and the price of power in the ComEd market when the price in PJM is \$0/MWh or less." (Direct Testimony of Bollinger, Goerss, Spilky, page 5, lines 110-114). RES Coalition

Witnesses Bohorquez, Boyle and Leigh explain that: 1) ComEd's MVI formula should recognize the cost of generation capacity; 2) the utilities should monitor forward price data and take appropriate corrective actions; 3) the MVI should account for liquidity risk; and 4) a placeholder for RTO charges should be utilized. (Direct Testimony of Bohorquez, Boyle, Leigh, page 5, lines 100-114). NEM urges the Commission, at a minimum, to adopt the RES Coalition proposals resulting in a 15 mill upward adjustment to permit the market value calculations to more adequately represent the full energy supply and commercial costs of serving retail load.

The utilities have attempted to recast the Commission-ordered focus of market value tariffs away from retail costs by focusing on "freed up electric power and energy," an inherently wholesale energy market-only concept. The utilities cloud the debate by arguing that accounting for the full energy supply and commercial costs of serving retail load would act as a subsidy for competitive marketers. For instance, ComEd Witness McNeil argues that,

"(f)actors that have been labeled retail margin, customer acquisition costs, retail electric power and energy sales and marketing costs, or retail marketing administrative costs relate to a RES's potential costs of doing business and have nothing to do with the market value of freed-up electric power and energy. I do not believe such factors are appropriate to consider in determining market values. We also do not have a way to estimate such costs in any reasonable way." (Direct Testimony of William McNeil, page 12, lines 231-236).

Similarly, ComEd Witness McDermott argues that, "the proposals for increasing the MVEC to recognize 'embedded costs' such as alleged retail marketing costs or making up for "residuals" from past prices are fundamentally at odds with the policy of fairly providing transition charge recovery for ComEd. By definition, the market value should

be a forward looking concept and should represent the value of the power and energy freed up from removing customers from the ComEd system." (Rebuttal Testimony of Karl McDermott, page 5, lines 105-110). RES Coalition Witnesses Gale and O'Connor refute this argument explaining that, "the continued advancement of the notion that the value to be determined is some sort of plain vanilla, wholesale "freed-up" value of energy is the only sure-fire way that a utility can hope to justify the continuation of the insufficiencies in the current MVI models." (Direct Testimony of Brent Gale and Philip O'Connor, page 9, lines 449-452). In the interest of promoting the development of a robust Illinois retail market, NEM urges the Commission to reaffirm that the market value calculations should not merely reflect wholesale prices but include the values associated with both full energy supply-related costs and the commercial costs of serving retail load.

#### **IV. Multi-year option issues**

##### **E. Limitation on load eligible for multi year TC contracts**

ComEd proposed a new Rider CTC-MY that would allow certain customers to lock-in their transition charges for a two-year period. (Direct Testimony of Paul Crumrine, page 16, lines 353-354). The availability of this Rider is proposed to be limited to customers that receive an individually calculated transition charge and is also limited to 500 megawatts of total load. (Direct Testimony of Paul Crumrine, page 16, lines 362-363, and page 17, line 374). NEM submits that the benefits inherent in Rider CTC-MY should not be limited in the manner proposed by ComEd.

RES Coalition Witnesses Gale and O'Connor note that, "[i]mposing limitations on the availability of a multi-year MVEC/CTC lock-in is inconsistent with the Company's own position of wanting to have certainty and move customers off system supply and into the competitive market." (Direct Testimony of Brent Gale and Philip O'Connor, page 38, lines 850-853). RES Coalition Witnesses Gale and O'Connor specifically recommend that,

"ComEd should not be allowed to limit the availability of a multi-year MVEC to customers for whom the provision of electric power and energy has been declared 'competitive.' It would be unreasonable in the extreme to prevent a customer from exercising a multi-year lock-in at the very same time that the Company is on course to phase out its supply obligation to that customer. Nor should the Commission apply a limit upon the availability of a multi-year lock-in for those customers currently taking service from RESs with 'flowed power.'" (Direct Testimony of Brent Gale and Philip O'Connor, page 39, lines 863-870).

The RES Coalition has identified an important segment of customers that are entitled to the benefits of Rider CTC-MY. The increased certainty provided by the Rider will permit customers and competitive suppliers to evaluate and enter into long-term agreements. This benefit should not be unnecessarily restricted.

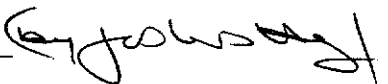
## **VII. Conclusion**

For the foregoing reasons, NEM urges the Commission, at a minimum, to upwardly adjust the market value by at least 15 mills to recognize the values associated with the utilities' affirmative obligation to maximize the value of capacity attributable to customers that migrate while managing, mitigating and minimizing the costs that would have been incurred in serving said customers. This result would be consistent with the legislative intent underlying the electric choice law as well as Commission Orders

pertaining to market value calculations. NEM also urges that the customer eligibility for ComEd's Rider CTC-MY be expanded as recommended by the RES Coalition.

Respectfully submitted,

THE NATIONAL ENERGY MARKETERS  
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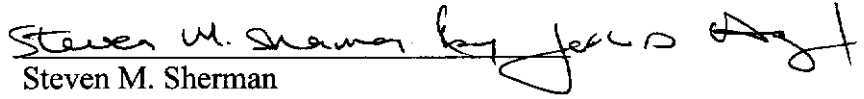
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Dated: January 28, 2003.

**CERTIFICATE OF SERVICE**

I, Steven M. Sherman, hereby certify that I served a copy of the INITIAL BRIEF OF NATIONAL ENERGY MARKETERS ASSOCIATION upon the service list for Docket Nos. Nos. 02-0656, 02-0671 and 02-0672 by e-mail on January 28, 2003.

  
Steven M. Sherman

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